

CHAPTER 14: REFINANCING WITH PRIVATE CREDIT [7 CFR 3550.160]

14.1 OVERVIEW

The Agency's loan programs are not intended to compete with or supplant private credit sources. To ensure that Section 502 loans are used only to assist borrowers unable to obtain credit from other sources, periodic reviews are conducted to determine borrowers' ability to refinance 100 percent of their Agency loans with private credit (formerly known as "graduation"). A borrower who fails to comply with requests for information to determine their ability to refinance, or who fails to refinance upon request by the Agency, is in default of the mortgage agreement and is subject to liquidation.

Centralized Servicing Center (CSC) Staff and Field Staff share responsibility for determining whether a borrower is able to refinance with private credit. Because Field Staff are in a better position to keep abreast of the underwriting criteria used by local lenders, the majority of the review process takes place at the Field Office. However, CSC is responsible for determining when a borrower will be reviewed, and for generating lists of borrowers for refinancing. This means that the process of reviewing borrower ability to refinance requires good communication and coordination between CSC and Field Staff.

14.2 SUBSEQUENT CREDIT

Borrowers under review for refinancing should not be considered for additional credit until the refinancing review is complete, unless the Agency determines that additional credit is necessary to protect the Government's interest in the property.

If Field Staff are in the process of reviewing a borrower's request for a subsequent loan when that borrower is selected for the refinancing review, the subsequent loan should be processed before initiating the refinancing review. If the review for the subsequent loan shows that the borrower would be able to get private credit for the amount of the subsequent loan, the borrower's request for a subsequent loan should be denied. The refinancing review should then be initiated to determine the borrower's ability to obtain credit to refinance the existing loan.

14.3 UNDERSTANDING LENDER POLICIES

Field Staff must be familiar with lending practices in their market areas in order to determine effectively whether an individual borrower will be a good candidate for refinancing with private credit. To stay current on this information, Field Staff should:

- Hold periodic meetings with lenders from mortgage companies, banks, and savings and loan associations to inform lenders about the Agency's refinancing policy and discuss the potential for the financial institution to work with Agency borrowers; and
- At least once a year, conduct a survey of local lenders to understand their lending policies using the survey included in Attachment 14-A.

The information gathered from lender meetings and surveys should be compiled into a list of lenders who have expressed an interest in refinancing Agency loans and/or lenders whose rates and terms appear reasonable. This list and any supporting information should be maintained in the operational file. Field Staff should provide the list of lenders to borrowers when they are asked to refinance with private credit. This will help ensure that they request credit from a lender who is interested in refinancing the loan, and who offers rates and terms that may meet the borrower's needs.

14.4 SUBORDINATION

When a borrower refinances a Section 502 loan, recapture will be calculated. The recapture may be paid at the time of refinancing, or if the borrower will continue to occupy the property, the Agency may subordinate its interest in any deferred recapture amount to facilitate a borrower's efforts to refinance with private credit, as long as: (1) the total value of all secured loans does not exceed the market value of the property; (2) the borrower continues to occupy the property; and (3) title does not transfer. The amount to which the Agency's loan may be subordinated can include:

- The amount required to repay the Agency debt, exclusive of recapture;
- Reasonable closing costs;
- Up to 1 percent of the loan amount for the lender's loan servicing costs; and
- The cost of any necessary repairs or improvements to the security property.

14.5 SELECTING BORROWERS FOR REVIEW

All Section 502 borrowers are considered for refinancing once every 2 years. For those borrowers receiving payment subsidy, the refinancing review will be scheduled around the time of the annual payment subsidy review to avoid requiring borrowers to provide duplicate information.

CSC reviews the borrower's payment history, income, and outstanding loan balance to predict whether the household will be able to refinance with private credit. If there is a reasonable likelihood that a borrower will be able to refinance based on the indicators available on FASTeller, the borrower is selected for further review.

A borrower's ability to refinance also may be reviewed any time the Agency becomes aware that a borrower's circumstances have changed. Such changed circumstances might include: an inheritance, a new job, or any other change that might lead to an increase in a borrower's income. Selection based on such information can be initiated either by CSC or Field Staff. The Agency must be consistent about initiating reviews when information is obtained that indicates a possible change in circumstances.



14.6 PROCESSING REFINANCING REVIEWS

A. Requesting Borrower Information

When a borrower is selected for a refinancing review, the Field Office will send *Handbook Letter 4(3550), Initial Request for Financial Information* to notify the borrower that the refinancing review is taking place and to request the information Field Staff will need to conduct the review. The letter will include *Form RD 1944-3, Budget and/or Financial Statement* for the borrower to complete and return. If there has been no recent payment subsidy review, the letter also will contain *Form RD 3550-1, Authorization to Release Information* for the borrower to complete and return.



Handbook Letters Used For Refinancing With Private Credit

Handbook Letter 4(3550), Initial Request for Financial Information

Handbook Letter 5(3550), Followup Request for Financial Information

Handbook Letter 6(3550), Notification that the Agency Will Continue With Loans

Handbook Letter 7(3550), Request for Borrower to Refinance With Private Credit

Handbook Letter 8(3550), Reminder Letter

Handbook Letter 9(3550), Confirmation of Determination that Borrower Must Refinance

Handbook Letter 14(3550), Final Notification to Submit Information for Refinancing Review

Handbook Letter 4(3550) instructs the borrower to return the completed forms to the Field Office within 30 days. If the borrower fails to respond, Field Staff must send *Handbook Letter 5(3550)*, *Followup Request for Financial Information* as a reminder, requesting that the borrower provide the required information within 15 days and notifying them that they will be in violation of their security instruments if they do not respond.

If the borrower's information has not been received 15 days after *Handbook Letter 5(3550)* is sent, Field Staff should attempt to make personal contact with the borrower to determine why the required information has not been provided, and to offer assistance, if appropriate. For example if the borrower is having difficulty completing *Form RD 1944-3*, *Budget and/or Financial Statement*, Field Staff should provide guidance.

The next appropriate action to take depends on the results of the followup contact.

- **Likely to submit.** If Field Staff determine that the borrower is likely to submit the required information, the borrower may be offered a grace period in which to provide it. The grace period is not usually more than 7 days. The reasons for the delay and the grace period offered should be documented.
- **Not likely to submit.** If Field Staff determine that the borrower is unlikely to submit the required information, the borrower will be considered uncooperative.



B. Acceleration for Uncooperative Borrowers

When a borrower is being uncooperative, aggressive action must be taken. This will include additional attempts to contact the borrower by telephone, as well as sending *Handbook Letter 14(3550)*, *Final Notification to Submit Information for Refinancing Review*. This letter notifies the borrower that failure to cooperate with the review is a violation of the security instruments. It also indicates that if the borrower fails to provide the required information to the Field Office within 15 days, the account will be accelerated.

If after sending *Handbook Letter 14(3550)*, the borrower makes a good faith effort to provide the necessary information, the Field Office will not request CSC to accelerate the account. A good faith effort might include sending a financial statement without the other required information, with an assurance that the rest will be provided within a reasonable time frame. If the borrower does not follow through the required materials, Field Staff should advise CSC to accelerate the account.

If the borrower submits the necessary information after the account has been accelerated, Field Staff will notify CSC and request that CSC hold the foreclosure actions in abeyance until the information can be adequately reviewed. If it is determined that the borrower is able to refinance, Field Staff should notify CSC that foreclosure actions should continue to be held in abeyance for an additional 90 days to provide the borrower adequate time to refinance. If the borrower fails to refinance within 90 days, or refuses to refinance upon request without good cause, Field Staff will notify CSC to continue with foreclosure actions. If the borrower submits information which demonstrates their inability to refinance, the acceleration will be canceled.

14.7 DETERMINING WHETHER REFINANCING IS REQUIRED

A. Reviewing Borrower Information

Once a borrower submits the requested information, Field Staff should review it to see if it appears that the borrower may be able to meet the rates, terms, loan fees, and conditions offered by private lenders. The income and assets of household members who are not parties to the note should not be considered when calculating ability to refinance with private credit, except that in community property states the spouse's income must be considered, even if the spouse is not a party to the note.

Field Staff can use UniFi to estimate whether the borrower is likely to be able to support a loan on the rates and terms available from private lenders by designating 100 percent participation by the lender. Field Staff also should consider whether the borrower has sufficient assets or equity in the property to pay charges that cannot be financed, and to meet any down payment requirements the private lender may impose.

If it appears, based on the information submitted by the borrower, that a private lender might refinance the loan, Field Staff should verify the household's repayment income. If a payment subsidy review has been conducted in the past 90 days, verification may be available through FASTeller. If not, Field Staff should follow the instructions in Chapter 4 to verify the household's income.

B. Taking Action on Borrower Information

Once the borrower's income has been verified, Field Staff should again use UniFi to assess the borrower's ability to refinance with private credit.

1. Borrowers Who Appear Unable to Refinance

If the review indicates that a borrower is unable to refinance with private credit, Field Staff should send *Handbook Letter 6(3550), Notification that the Agency Will Continue With Loans* indicating that the Agency will continue with the loan and that the borrower's ability to refinance will be reviewed again in 2 years.

2. Borrowers Who May Be Able to Refinance

If the review indicates that the borrower may be able to refinance, Field Staff must send *Handbook Letter 7(3550), Request for Borrower to Refinance With Private Credit* to request that the borrower refinance with private credit within 90 days of the date of the letter. The letter notifies the borrower of the amount of principal and interest to be refinanced and the maximum amount of subsidy that may be subject to recapture. Field Staff should attach to *Handbook Letter 7(3550)* a list of at least 2 lenders that are likely to offer the borrower private credit. *Handbook Letter 8(3550), Reminder Letter* must be sent 45 days later to remind the borrower of the 90 day deadline.

14.8 BORROWER RESPONSES

A. Contesting the Agency Decision

The borrower has 30 days from the date of *Handbook Letter 7(3550), Request for Borrower to Refinance With Private Credit*, to contest the Agency's determination and to provide additional documentation for the Agency to use in reconsidering the decision. Field Staff should review such documentation within 7 days of receiving it. If the Field Staff's determination that the borrower should be able to refinance does not change, the borrower must be sent *Handbook Letter 9(3550), Confirmation of Determination that Borrower Must Refinance* to confirm that refinancing will be required. If Field Staff find that the additional information indicates that the borrower cannot refinance, the borrower must be sent *Handbook Letter 6(3550), Notification that the Agency Will Continue With Loans*.

B. Borrowers Who Find Private Financing

Handbook Letter 7(3550) instructs borrowers who the Agency has determined capable of securing private credit to contact CSC for a final payoff amount and instructions about determining recapture, making the final payment, and/or deferring recapture amounts.

C. Borrowers Who Do Not Find Private Financing

Borrowers who are unable to secure private credit must provide a rejection letter from at least 1 lender included on the list of lenders sent with *Handbook Letter 7(3550)*. The letter must contain the following information:

- The lender's name;
- The amount of the loan requested;
- The information the borrower provided to the lender regarding the purpose of the loan; and
- The rates and terms offered by the lender, and the specific reasons why credit was denied.



Differences in Interest Rates

A difference in interest rates between the Agency's loan and loans offered by private lenders is not a sufficient reason for a borrower to fail to refinance.

Field Staff should review the lender's rejection letter to ensure that the loan the borrower requested was for the appropriate amount, purpose, and term. For example, a letter that indicates that the borrower was rejected for a loan for more than the outstanding Agency debt, or for a loan term shorter than typically offered, would not adequately demonstrate an inability to refinance.

If the rejection letter is sufficient to document the borrower's inability to refinance, Field Staff should send *Handbook Letter 6(3550)* to notify the borrower that refinancing will not be required. If the evidence does not demonstrate the borrower's inability to refinance, Field Staff should send *Handbook Letter 9(3550)* to reiterate the requirement that the borrower refinance before the end of the initial 90 day deadline. The 90 day time frame is not extended for borrowers who are rejected for unacceptable reasons.

Borrowers who have been asked to refinance and fail to do so within 90 days are in violation of the security instruments. This is considered a nonmonetary default, and must be referred to CSC for acceleration. Field Staff must provide CSC with the documentation needed to develop a problem case report, including the *Form RD 1944-3, Budget and/or Financial Statement*, if available, and copies of all letters the Agency has sent to the borrower pertaining to the refinancing request.

ATTACHMENT 14-A
SURVEY OF LENDER CREDIT CRITERIA

BACKGROUND INFORMATION

Date: _____

Name of Organization: _____

Name and Title: _____

Address: _____

Service Area: _____

1. Are you interested in making loans to refinance the loans of RHS borrowers?

Yes ☐ No ☐

If you are interested, but not at this time, when would be a more appropriate time?

2. How much credit do you expect to have available in the next 3 to 4 months for making such loans? _____

In the next 12 months? _____

3. What are your loan terms? _____

4. What is your current interest rate? _____

Variable Rate ☐ Fixed Rate ☐

5. Is a risk differential used in establishing interest rates charged for new borrowers?

Yes ☐ No ☐

If yes, please explain. _____

6. What can a typical loan applicant be expected to pay for:

- A. Filing an application \$_____ or _____%
- B. Real estate appraisal \$_____ or _____%
- C. Credit report \$_____ or _____%
- D. Loan origination fee \$_____ or _____%
- E. Loan closing costs \$_____ or _____%

7. Is mortgage guarantee insurance required?

Yes ☐ No ☐

If yes, how many years?_____ What are the costs?_____

8. Is there a minimum or maximum loan size policy?

Yes ☐ No ☐

If yes, please explain._____

9. Are there minimum and maximum home values?

Yes ☐ No ☐

If yes, minimum? \$_____ Maximum? \$_____

10. What loan to market value ratio do you require?_____

11. Are there minimum net and gross income criteria? If yes, what are the criteria?

Yes ☐ No ☐

If yes, net? \$_____ Gross? \$_____

12. Do you use a minimum loan or home value to income ratio?

Yes ☐ No ☐

If yes, what is the loan to income ratio? _____

Value to income ratio? _____

13. Is there a maximum percentage of gross income a typical applicant may have to pay for:

A. Principal, interest, taxes, and insurance (PITI)? _____%

B. Total housing costs and other debt obligations? _____%

14. Do you have any policies regarding age of home, housing type, site size, or service area?

Yes ☐ No ☐

If yes, please list. _____

15. Other comments: _____

